IS NO TARGET TOO BIG? CONSORTIUM BREAK-UP BIDS IN A POST-ASCIANO WORLD

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Legal Briefings – By **Rebecca Maslen-Stannage**, **Philippa Stone**, **Courtney Dixon** and **Alice Gardoll**

A consortium break-up bid involves a consortium acquiring a target, and breaking up and sharing the target's assets upon implementation of the deal.

As well as reducing the equity cheque and level of debt required by a bidder, consortium break-up plays can overcome ACCC, FIRB and other regulatory issues by allocating key assets to consortium members which are acceptable to the relevant authority.

Stamp duty and tax obstacles, as well as analysis of contractual change of control triggers, are key in the analysis - and may rule out particular break-up plays.

THE ASCIANO CONSORTIUM BREAK-UP BID

The Brookfield / Qube consortium's acquisition of Asciano by scheme of arrangement involved a special purpose vehicle (**BidCo**) acquiring all the shares in Asciano.

The structure of the Asciano bid reflects a typical 'consortium break-up bid', under which two or more companies or groups form a consortium to acquire a target with a view to splitting up the target after completion. Asciano involved the union of two bidding groups in a consortium following fierce bidding between the bidders to take over Asciano in their own right.

The deal provided for the effectively contemporaneous break-up of Asciano into three separate companies, reflecting Asciano's business units. Under the scheme, shares in Asciano were acquired by BidCo on the basis that BidCo would be owned by a Rail consortium (led by GIP and CPPIB), which would retain Asciano's Pacific National rail business. The deal was conditional upon two "connected transactions": the sale of Asciano's ports and Bulk and Automotive Port Services (**BAPS**) businesses each to a smaller consortium within the larger consortium, with PortsCo to be co-owned by Qube and Brookfield (and Brookfield's consortium partners) and BAPSCo to be owned by Brookfield (and its consortium partners).

As a result of this structure, Qube and Brookfield gained exposure to different aspects of the Asciano business. In this way, a consortium break-up bid provided for the acquisition of a large target, but also allowed consortium members to each break off a smaller entity which the relevant consortium member then controlled.

WHY A CONSORTIUM BID?

It is not uncommon for a potential target to have some assets which the bidder doesn't want and would rather not pay for. For example, in Metcash's 2004 takeover bid for Foodland, Metcash only wanted Foodland's Australian business, not its New Zealand assets. To structure this as a sole bidder required an elaborate bid structure, with an embedded pre-blessed in specie capital reduction under which – post-bid – Metcash would spin Foodland's New Zealand business back out to the former Foodland shareholders through a capital reduction.

Ultimately in that case, Woolworths emerged as a willing bidder for Foodland's New Zealand business. Under pressure from its shareholders to maximise value where different bidders wanted different assets, Foodland demerged itself into Foodland Australia – which was acquired by Metcash under a scheme of arrangement, and Foodland New Zealand – which was acquired by Woolworths. Theoretically, a consortium bid by Metcash and Woolworths could have been an alternative way of structuring that even on a hostile basis – with a simpler structure than the Metcash takeover bid.

Another reason for a consortium bid is to overcome regulatory issues – if one bidder has competition issues with a particular asset held by the target, having a consortium partner who can take that asset may be a neat solution. In Asciano, the ACCC had raised issues with Brookfield acquiring Asciano's Rail business and also with Qube (or a Qube funded vehicle) acquiring Asciano's BAPS business – the final 'break-up' structure solved both those problems, and also (because funding requirements were spread over a larger group of investors) permitted an all cash bid to be offered to Asciano shareholders (compared to cash and scrip under each of the previous rival bids). With the ACCC increasingly requiring "fix it first" divestment solutions rather than allowing a bidder to acquire, ringfence and divest post-acquisition (which of course brings its own risks), the ability to have another consortium member who will take that asset at the point of completion could make the difference between being able to bid or not, including on a hostile basis. Of course if the consortium includes competitors, care is needed not to breach the competition laws in the bid itself. Through careful structuring and protocols this should usually be do-able.

It's not hard to envisage circumstances where a FIRB approval issue could be overcome through a similar structure, with the contentious asset allocated to an Australian consortium member, and the foreign consortium member being able to obtain approval to acquire the balance of the target on that basis.

Launching a consortium bid can be an effective way to mitigate commercial or deal risk for a bidder who has plans to sell off part of the target's business – whether by regulatory imperative or for commercial reasons. It can give the bidder execution and price certainty on that disposal from the outset rather than having to carry market and execution risk – and in a way which is more appealing to target shareholders than some form of break-up bid which leaves them with part of the asset. At the same time, there may be a defensive benefit – by including the logical buyer of that asset in the consortium this can forestall a rival bid by that party. It's better for both parties to make a consortium bid and share the assets between them.

WHEN WON'T THE CONSORTIUM BREAK-UP PLAY WORK?

We sometimes see shareholder activists propose that companies break themselves up with a view to delivering value to shareholders, but detailed analysis shows that the damage done by the break-up outweighs the positives. This could be for commercial reasons (e.g. dis-synergies, or contractual change of control triggers which could lead to loss of important contracts or joint ventures or trigger repayment of corporate group debt) or because of stamp duty and tax consequences – which can be considerable and, in some cases, prohibitive. It very much depends on the structure and history of the assets.

These factors make due diligence even more critical (as of course it is in any takeover), and if the bid is hostile the bidder needs to consider appropriate conditions to protect it if issues emerge during the bid process which make the break-up more costly, or otherwise less appealing, than initially anticipated.

OTHER EXAMPLES OF CONSORTIUM BREAK-UP BIDS

While Asciano has certainly been one of the largest high profile Australian deals utilising a consortium break-up bid, previous examples of this structure include:

- *Carlsberg / Heineken for Scottish & Newcastle:* a large scale international example of a consortium break-up bid is the 2008 £7.8 billion acquisition of brewers Scottish & Newcastle (**S&N**) by Carlsberg and Heineken. The consortium acquired S&N by scheme of arrangement through a special purpose vehicle, and then split the company's assets by geography, with Heineken acquiring its British, Indian, US and other operations, and

Carlsberg securing Baltic Beverages Holding, a joint venture between it and S&N, and a number of assets in Europe and Asia. Heineken and Carlsberg jointly operated BidCo as a 50:50 venture, and contributed to the acquisition price at 44.1% and 55.9% respectively.

- *Babcock & Brown* (and various managed funds) and Singapore Power for Alinta Energy in August 2007: a consortium led by Babcock & Brown and Singapore Power agreed to acquire Alinta Energy by scheme of arrangement (following a bidding process against a Macquarie led consortium) and to divide Alinta's assets among the consortium members (including a number of Babcock managed funds which also contributed scrip consideration), based on the acquiring entities' different business focuses.

- *Healthscope / Ironbridge Capital and Archer Capital for Symbion Health:* the bid by Healthscope for Symbion Health in May 2007 involved a consortium-like structure. Healthscope offered to acquire Symbion, by scheme of arrangement, for cash and Healthscope shares. While Healthscope sought to acquire Symbion alone, the plan was for Symbion's Pharmacy Services and Consumer businesses to be sold to a consortium comprising Ironbridge Capital and Archer Capital following Healthscope's acquisition.

- *Macquarie Media / Fairfax Media for Southern Cross Broadcasting:* Macquarie Media and Fairfax Media formed a consortium in 2007 to acquire Southern Cross Broadcasting by scheme of arrangement. Macquarie Media and Fairfax agreed that, following implementation of the scheme, Fairfax would acquire Southern Cross' radio businesses (along with a number of other entities), while Macquarie Media would hold Southern Cross' regional television operations. Although smaller in monetary terms than Asciano, this deal featured a key characteristic which lends a deal to a consortium break-up bid: a target with a distinct and diverse range of assets, each of which interests different consortium members.

- *Smorgon / OneSteel for Email Limited:* Smorgon Steel Group Limited made a number of unsuccessful bids for Email Limited throughout 2000 before entering into a successful joint bid with competitor OneSteel. The consortium bid involved amending Smorgon's pre-existing bid so that the acquiring company, a subsidiary of Smorgon, would be jointly owned by Smorgon and OneSteel. The consortium's bid was conditional on Email selling off its Major Appliances business, and was followed by the spin-off of all of Email's non-core businesses by 2003, leaving the consortium with the metals businesses that it intended to acquire.

CONCLUSION

The ultimate success of the consortium break-up bid for Asciano may embolden bidders to look at larger targets with distinct assets or businesses that lend themselves to being broken down. Perhaps they might see going straight to a consortium bid as more appealing than running the gauntlet of regulatory hurdles such as potential ACCC and FIRB objections, or as an overall commercial risk mitigant. Major companies which have thought of themselves as too big to take over may wish to assess whether this dynamic puts them more at risk of an unsolicited bid than might have been the case in the past, or alternatively whether this type of approach opens up further strategic opportunities to create value for shareholders.

** Herbert Smith Freehills acted for Brookfield, Metcash and Fairfax Media on the transactions discussed above.*

KEY CONTACTS

If you have any questions, or would like to know how this might affect your business, phone, or email these key contacts.

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